QUESTION PRESENTED

Whether joint rate filings by title insurance rating bureaus, authorized by state law, were "actively supervised" for purposes of the state action doctrine where (1) the state insurance departments had plenary power to review and disapprove the rates, (2) state laws granted the regulators the power and duty to regulate pursuant to standards that were enforceable in the state courts, (2) programs of supervision by state regulators were in place, staffed and funded, and (4) the regulators demonstrated a basic level of activity in carrying out the policies of the States, including reviewing the reasonableness of the filed rates.

RULE 29.1 LISTING OF PARENT COMPANIES, SUBSIDIARIES AND AFFILIATES

The Rule 29.1 listing of parent companies, subsidiaries and affiliates is included in Respondents' Brief in Opposition to the Petition for Certiorari and remains current, except as follows:

Respondent Lawyers Title Insurance Corporation is now a wholly-owned subsidiary of Lawyers Title Corporation, a publicly-owned corporation. No non-wholly-owned subsidiary or affiliate of Lawyers Title Insurance Corporation has publicly traded common stock.

The list of non-wholly-owned subsidiaries and affiliates of respondent Stewart Title Guaranty Company included in the Appendix to Respondents' Brief in Opposition to the Petition for Certiorari is amended to reflect the additions and deletions listed in the Appendix hereto.

TABLE OF CONTENTS

TABLE OF CONTENTS—Continued

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

No. 91-72

FEDERAL TRADE COMMISSION,
Petitioner,

v.

TICOR TITLE INSURANCE COMPANY, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Third Circuit

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BRIEF FOR THE RESPONDENTS

STATEMENT OF THE CASE

This Court must determine in this case whether the state action doctrine of federal antitrust law requires an antitrust court to conduct an intrusive, qualitative assessment of state economic regulation. In the decision below, the United States Court of Appeals for the Third Circuit reversed an order of the Federal Trade Commission, which had held that the Respondents violated the federal antitrust laws by participating in state-licensed rating bureaus that filed rates with state insurance regulators. *Ticor Title Ins. Co. v. F.T.C.*, 922 F.2d 1122 (3d Cir. 1991) (Pet. App. 1a-40a), *cert. granted*, 112 S.Ct. 47 (1991). The Court of Appeals held that the regulatory program existing in each State constituted "active supervision" under the standard enunciated by this Court in

California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc., 445 U.S. 97 (1980) ("*Midcal*").[1]

1. History Of This Proceeding.

The Third Circuit determined, with respect to the four States in which application of the state action doctrine depended on satisfying the active supervision requirement,[2] that the standard applied by the Federal Trade Commission ("FTC" or "Commission") "would, in effect, try the state regulator." (Pet. App. 32a.) It held that the "principles of federalism and state sovereignty that undergird the [state action] doctrine prohibit its selective application only where states act in a manner that a federal agency or federal court finds to be preferable." (Pet. App. 37a.) The Third Circuit held that, as articulated by this Court, active supervision requires only that state officials "have and exercise power to review particular anticompetitive acts of private parties and disapprove those that fail to accord with state policy." (Pet. App. 26a, *quoting Patrick v. Burget*, 486 U.S. 94, 101 (1988) ("*Patrick*")).

Applying this principle, the Third Circuit employed the test used by the First Circuit in reviewing another of the

[1] In *Midcal*, this Court held that acts of private persons are within the protection of the state action doctrine if the actions are taken pursuant to "clearly articulated and affirmatively expressed state policy," and are "actively supervised" by the State. 445 U.S. at 105.

[2] Arizona, Connecticut, Montana and Wisconsin. In two other States (New Jersey and Pennsylvania) the Commission had held that the "clearly articulated state policy" requirement of *Midcal* was not satisfied because the state insurance regulators had exceeded the scope of their regulatory authority under state law. (Pet. App. 149a-52a.) However, in light of the intent of those States to broadly regulate title insurers and the consistent construction of state law by the state agencies charged with its enforcement, the Third Circuit reversed the Commission and found the state regulators' interpretations of their own laws "worthy of our deference." (Pet. App. App. 20a.) The Commission does not challenge this holding before this Court.

FTC's rating bureau cases: does the state agency have "the authority to 'review particular anticompetitive acts of private parties and disapprove those that fail to accord with state policy,'" and does the agency "review[] the reasonableness of the [filed] rates." (Pet. App. 28a, *quoting New England Motor Rate Bureau, Inc. v. F.T.C.*, 908 F.2d 1064, 1071 (1st Cir. 1990) ("*New England*")). Concurring with the First Circuit that the FTC was "too demanding in the showing it would require as to the rigor and efficiency of a particular state's regulatory program," *id.*, the Third Circuit held that a State had exercised its regulatory powers where the following could be shown:

> Where . . . the state's program is in place, is staffed and funded, grants to state officials ample power and the duty to regulate pursuant to declared standards of state policy, is enforceable in the state's courts, and demonstrates some basic level of activity directed towards seeing that the private actors carry out the state's policy and not simply their own policy, more need not be established.

(Pet. App. 28a, *quoting New England*, 908 F.2d at 1071).

The Third Circuit concluded that the active supervision requirement was satisfied in each State. Regulators in Arizona, Connecticut, Montana and Wisconsin had authority to review and to disapprove filed rates. The Third Circuit also concluded that regulators in each of these States had exercised their power to control collective rate filing by reviewing the reasonableness of the filed rates under state statutory criteria. Each of the States granted to its insurance department ample power and the duty to regulate pursuant to declared standards of state policy, a duty enforceable in the States' courts. In each of the four States there was a program of supervision in place which was staffed and funded. Finally, in each of the States the insurance department had demonstrated some basic level of activity directed toward seeing that "the private actors carry out the State's policy and not simply their own policy." (Pet. App. 29a-38a.)

2. The Record Of State Supervision.

To evaluate the Commission's argument that the State programs at issue here failed to satisfy the active supervision requirement, it is necessary to consider the nature of the programs. This section addresses these programs, first, according their statutory requirements, and second, according to the actual activity of the state agencies.

a. *Statutory Scheme Of Regulation.*[3]

Each of the States at issue required title insurers to file title insurance rates, including rates for search and examination services, with the state insurance department.[4] Each State permitted these rates to be filed by an individual insurer or by a state licensed rating bureau.[5] The statutes of each State included detailed provisions pertaining to the organization and licensing of title insurance rating bureaus.[6] Each insurance department had the authority to revoke or to suspend the license of a rating bureau.[7]

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[3] This discussion focuses upon only the key components of the rate regulatory statutes applicable to title insurers in these four States during the relevant time period. State statutory provisions that are particularly relevant are reproduced in the Joint Appendix ("J.A.") at 166-211. Statutory provisions made part of the administrative record below are incorporated in the single joint hearing exhibit (*see* FTC Docket Sheet at 18).

[4] Ariz. Rev. Stat. Ann. § 20-376(A) (J.A. 168); Conn. Gen. Stat. Ann. § 38-201x (J.A. 183-84); Mont. Code Ann. § 33-16-203 (J.A. 195); Wis. Stat. Ann. § 625.13(1) (J.A. 207).

[5] Ariz. Rev. Stat. Ann. § 20-376(B) (J.A. 168); Conn. Gen. Stat. Ann. § 38-201d (J.A. 174); Mont. Code Ann. § 33-16-203 (J.A. 195); Wis. Stat. Ann. § 625.13(1) (J.A. 207).

[6] Ariz. Rev. Stat. Ann. §§ 20-361, 20-376(B) (J.A. 168); Conn. Gen. Stat. Ann. §§ 38-201d, 38-201j (J.A. 174); Mont. Code Ann. § 33-16-401 to 33-16-403 (J.A. 198-201); Wis. Stat. Ann. §§ 625.31-625.34 (J.A. 209-11).

[7] Ariz. Rev. Stat. Ann. § 20-374; Conn. Gen. Stat. Ann. § 38-201p(d) (J.A. 179-81); Mont. Code Ann. §§ 33-16-111, 33-16-112 (J.A. 192-93); Wis. Stat. Ann. § 625.32(4) (J.A. 211).

In each of the four States, rates were required to be not "excessive, inadequate or unfairly discriminatory."[8] By statute, proposed rates were effective (immediately or within a specified period) if the state agency took no affirmative action to challenge them.[9] The departments were required generally to enforce the provisions of the codes, and specifically to disapprove or rescind any proposed or effective rate which did not comport with the rate criteria.[10] Persons aggrieved by any rate filing were provided with specific statutory rights to require the regulator to hold a hearing or otherwise review the filing to determine that it comported with the rate criteria.[11]

Detailed statutory provisions explained the meaning of the statutory rate criteria.[12] In each State, the insurance department was authorized to develop statistical plans for the reporting of loss and expense experience, and to obtain the assistance of the rating bureau in collecting data on revenues and costs in order to assist the regulator in reviewing title insurance rates.[13] Each State's

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[8] Ariz. Rev. Stat. Ann. §§ 20-375(A), 20-376(D) (J.A. 167-68); Conn. Gen. Stat. Ann. § 38-201x(b)(2) (J.A. 186); Mont. Code Ann. §§ 33-16-201 (J.A. 193-94); Wis. Stat. Ann. § 625.11 (J.A. 205-06).

[9] Ariz. Rev. Stat. Ann. 20-376(E) (J.A. 168); Conn. Gen. Stat. Ann. § 38-201x(a)(2) (J.A. 184); Mont. Code Ann. § 33-16-203 (J.A. 195); Wis. Stat. Ann. § 625.13 (J.A. 207).

[10] Ariz. Rev. Stat. Ann. §§ 20-375(A), 20-376(D) (J.A. 167-68); Conn. Gen. Stat. Ann. §§ 38-4, 38-201p(b), 38-201x(b)(2) (J.A. 171, 178, 186); Mont. Code Ann. §§ 33-1-311, 33-16-205 (J.A. 188, 196); Wis. Stat. Ann. §§ 601.41(1), 625.22 (J.A. 201, 208).

[11] Ariz. Rev. Stat. Ann. § 20-378(B) (J.A. 170-71); Conn. Gen. Stat. Ann. § 38-201p(a), (b) (J.A. 177-78); Mont. Code Ann. §§ 33-16-204, 33-16-205 (J.A. 196-97); Wis. Stat. Ann. § 227.42(1).

[12] Ariz. Rev. Stat. Ann. § 20-375 (J.A. 167); Conn. Gen. Stat. Ann. § 38-201c (J.A. 172-73); Mont. Code Ann. § 33-16-201 (J.A. 193-94); Wis. Stat. Ann. §§ 625.11, 625.12 (J.A. 205-07).

[13] Ariz. Rev. Stat. Ann. § 20-371; Conn. Gen. Stat. Ann. § 38-201m(b) (J.A. 174-75); Mont. Code Ann. § 33-16-202 (J.A. 194-95); Wis. Stat. Ann. § 625.34 (J.A. 211).

statutory regime also provided standards and procedures for the filing of rates and rate justifications by rating bureaus.[14]

b. *Administrative Record Of Supervision.*

The following description of the state regulatory history is based on the findings of the Administrative Law Judge ("ALJ") adopted by the Commission, as well as the uncontradicted record evidence.[15] Beginning as early as 1965 until the FTC complaint was filed in January 1985, Respondents and other title insurers elected the option afforded by state statutes to make required rate filings through state licensed rating bureaus in Arizona, Connecticut, Montana and Wisconsin. (Pet. App. 217a.)

(1) Arizona. The initial rate filing of the Arizona rating bureau in 1968 was based upon an existing, competitively-determined rate structure, a type of filing expressly approved by state law. That filing was in effect for fifteen years until the bureau ceased to exist. During that period, the rate bureau also filed various forms and endorsements.

The bureau was founded in 1968 and made its first rate filing that year, pursuant to a new statute that for the first time required title insurance rates to be filed with the insurance department pursuant to regulatory criteria requiring that rates not be excessive, inadequate

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[14] Ariz. Rev. Stat. Ann. §§ 20-376, 20-377 (J.A. 168-70); Conn. Gen. Stat. Ann. § 38-201x (J.A. 183-88); Mont. Code Ann. § 33-16-203 (J.A. 183-88); Wis. Stat. Ann. § 625.13 (J.A. 207).

[15] In the following discussion, references to evidence in the FTC administrative record are made as follows: Testimony of witnesses at the administrative hearing is cited by the name of the witness and the page of the hearing transcript at which the testimony may be found (*e.g. Wilkie* 2071). Commission exhibits and respondents' exhibits admitted to the administrative record are cited by their prefix, exhibit number and page according to the numbering system used in the administrative hearing (*e.g.* CX 8, RX 502S). The page number of the Joint Appendix is also included for testimony or exhibits reproduced there (*e.g.* J.A. 47-50).

or unfairly discriminatory. Ariz. Rev. Stat. Ann. § 20-375(A) (J.A. 167). The rate regulation law grew out of concern over the solvency and stability of title insurers after the failure of two Arizona title insurance firms in the middle 1960's. (*Wilkie* 2071, J.A. 29.) The ALJ found that the rate structure proposed in the 1968 filing adopted, with slight modifications, pre-rating bureau competitive industry rates. (Pet. App. 202a n.233; *accord Wilkie* 2074-75, J.A. 30-31.) These rates were supported by express statutory language permitting rates to be justified for conformance with the state regulatory criteria on the basis of the actual experience of any title insurer or rating organization. Ariz. Rev. Stat. Ann. § 20-377 (J.A. 169-70).

The 1968 rate filing was accepted by the department without further inquiry to the bureau. (CX 8; RX 60A, J.A. 102-03.) The bureau then began to collect information concerning industry profitability which it could use to demonstrate to the department on a regular basis that the rates were not excessive, inadequate or unfairly discriminatory, and therefore conformed to the statutory criteria. Contacts were made with experts familiar with title insurance rate regulation in other States, and a rate justification committee of the bureau compiled income and expense statistics from most of the Arizona title insurance industry for the years 1966-70. (*Wilkie* 2077-79, J.A. 32-33; RX 60A, J.A. 102-03.)

In 1971, the department convened a hearing to consider, among other matters, "[t]he basis upon which rates and fees currently charged the public . . . are fixed; and . . . [t]he rating material currently on file with the Department." (RX 72, J.A. 106.) At the hearing, the bureau submitted to the department its collected data concerning industry profitability for the period from 1966 to 1970. (*Wilkie* 2082-83, J.A. 34-35.)

Beginning in 1971, the bureau hired the accounting firm of Ernst & Ernst to collect income and expense in-

formation. Through 1977, Ernst & Ernst collected information on a yearly basis that was retained by the bureau to support the reasonableness of the rate structure. (*Wilkie* 2078-79, J.A. 32-34.) The bureau president testified that "[w]e felt that we should have [the information] available in the event [it was] required by the department or, in the event that we deemed that we wanted to go in and have a rate hearing." (*Wilkie* 2080, J.A. 34.)

In 1977, the bureau filed rates for escrow services pursuant to a statutory amendment which brought such fees within the regulatory structure. Department officials warned the bureau that it "would have to be in a position to substantiate [any escrow fee] filing" and that the appropriateness of the level of escrow rates would be judged by the department in light of the existing title insurance rates. (*Wilkie* 2092-93, J.A. 35-36.) The escrow rates submitted by the bureau continued the approximate historical rate of return, and "were basically no change from that generally being charged by the industry at that time." (*Id.* 2095-96, J.A. 37-38.) In recognition of the short time period within which the new rates were required by statute to be filed, the department accepted the filed rates, conditioned upon proof that the bureau had retained Arthur D. Little, Inc. ("A.D. Little") to develop a program to collect further information to support the reasonableness of the rate structure. (*Wilkie* 2095, J.A. 38.)

A.D. Little developed financial and statistical reporting plans to assess the overall profitability of the Arizona title insurance industry.[16] (*Plotkin* 2406, 2473-75, 2483-

[16] A.D. Little, the economic consulting firm (*see Plotkin* 2377, J.A. 60-61), created a data collection and reporting system which was used by regulators in more than seventeen States (*Plotkin* 2490, J.A. 64), including Arizona, Connecticut, and Wisconsin. Its system included a financial or income and expense reporting plan to provide the state regulator a method for determining the overall rate of return achieved by the title insurance industry in a particular State, which could be compared with other States and industries. (*Plotkin* 2473-83, J.A. 61-63.) The system also included a separate statistical plan to assist the regulators in assessing the impact of a rate structure upon different classes of consumers; *viz.*, whether the rate is not discriminatory. (*Plotkin* 2483-88, J.A. 63-64.)

The A.D. Little financial reporting plan was intended to assess the profitability of title insurers under the overall rate structure, not to cost-justify particular segments of the rates. In A.D. Little's view, the nature of the title insurance business and rate structures would make any attempt to cost-justify particular segments of the rates "extremely arbitrary." (CX 91Z-103, J.A. 101.) Among the factors cited for this view were the small loss ratio in title insurance, the high proportion of fixed costs, and the fact that title insurance rate structures "reflect primarily legislative and regulatory social policies, historical practice, and the realities of the product market." *Id.*

85, J.A. 61-64.) Dr. Plotkin of A.D. Little testified that the development of the plans in Arizona involved an interactive process with the department, in which the director himself was involved. (*Id.* 2611, 2624, J.A. 67, 71.) Beginning in 1978, A.D. Little prepared and submitted annual reports examining the profitability of the Arizona title insurance industry, which included data for the years from 1972 to 1980. (RX 88; RX 91; RX 92; RX 493.) The A.D. Little reports showed the rates in these years were not excessive or inadequate. (*Plotkin* 2610, 2619-20, J.A. 67-70.)

In November 1980, the department decided to conduct an examination of the bureau by an outside consultant, at the bureau's expense, focusing on rates, ratemaking procedures, competition, and the A.D. Little methodology for measuring profitability. (RX 93-93B, J.A. 108-11.) The examination was conducted by the actuarial firm of Tillinghast, Nelson & Warren, which was chosen by the department. The Tillinghast examination included review of the A.D. Little plans and results, a general critique of the bureau ratemaking procedures and the background and nature of title insurance generally. (*Bethel* 1910-11, 1974-76, J.A. 23-26.)

The Tillinghast report, completed in 1982, endorsed the A.D. Little reports and agreed with the A.D. Little conclusion that the bureau rates from 1972-80 were not excessive, though it suggested that by the time of the 1981 real estate recession the rates might have been inadequate. (RX 96-96H; RX 96J; *Bethel* 1975, J.A. 26.) The witnesses familiar with the department's policies uniformly testified that if the rates had been shown to be excessive, the department would have acted promptly to rectify the situation. (*E.g. Bethel* 1981-82, J.A. 27-28; *Barberich* 2261-62, J.A. 52-53.)

Between 1968 and 1980 the bureau filed a number of what the FTC found to be "minor" rate amendments, adjustments and endorsements. (Pet. App. 67a.) Department employees in charge of reviewing rate filings since 1973 testified that department policy was to review every filing for conformance to the statutory criteria and seek supporting information if it was deemed necessary. (*Barberich* 2230-34, J.A. 47-50; *Williamson* 2190, J.A. 43-44.) The FTC found that the record was "inconclusive" as to the review that these filings actually received. (Pet. App. 67a.)

Members began to withdraw from the bureau following entry of judgment in December 1981 in an antitrust suit brought by the United States Department of Justice challenging the bureau's filing of collective rates for escrow services. (Pet. App. 205a; *Wilkie* 2102, J.A. 39; *Plotkin* 2621-22, J.A. 70-71.) The bureau's corporate charter was revoked in 1983. (Pet. App. 205a.)

(2) Connecticut. The Connecticut rating bureau made two general rate filings, in 1966 and 1981. In addition, the bureau filed numerous amendments and endorsements from 1966 to 1983.

The ALJ found that in response to the 1966 filing, the department sought additional justification from the bureau. (Pet. App. 191a; RX 104, J.A. 112-13.) After soliciting the assistance of its members to gather the

requested information (RX 105, J.A. 114-15), the bureau withdrew its original filing (RX 106, J.A. 117), and submitted, in response to the department's inquiry, a new filing that included a proposed rate manual, proposed policy forms, and a memorandum explaining and supporting the revised filing (RX 107-107a, J.A. 118-19). Upon requesting additional information concerning the revised filing (RX 108, J.A. 120), the department acknowledged receipt of the filing and additional correspondence (RX 110, J.A. 124). According to the ALJ, the department then "approved the bureau's rate, effective August 15, 1966," (Pet. App. 191a; RX 110, J.A. 124), although the ALJ determined that there was no evidence that the request for justification was ever answered "satisfactorily," (Pet. App. 191a).

On December 3, 1981, the bureau filed its only other major rate filing. (Pet. App. 192a.) Prior to this filing, department and bureau representatives met to review the perceived need for the increase and to determine what information would be necessary to support it. (*Ferraro* 2311-13, J.A. 58; *DiSanto* 2737, J.A. 75.) The department discussed with the bureau the level of agents' commissions in Connecticut (*DiSanto* 2737-41, J.A. 75-77), which the department had no authority to regulate directly, (*DiSanto* 2739-41). "[D]iscussion centered around alternatives . . . as to what steps could be taken to effectively bring forth a reduction in [agent] commission[s], as a means of lowering the cost of title insurance [to] the consumer." (*DiSanto* 2788.)[17] Follow-

[17] The subject of agents' commissions had been discussed by the Department with representatives of the title insurance industry in prior occasions. (*DiSanto* 2739, J.A. 76) (the agency commission issue "has been kind of a constant item for discussion when I meet with or when I had met with title insurance people, the rating organization member representatives"); (*DiSanto* 2756, J.A. 79). *See also* RX 114-114A (J.A. 125-26) (discussing the department's indication that it might seek to limit amount of commissions paid to agents).

ing these discussions the department determined that the level of commissions paid to agents was not the result of actions by the bureau or its members, but rather was controlled by the competitive market for agents, which was unregulated, and in which title insurers competed to obtain business. (*See, e.g., DiSanto* 2798-2800.)

The department closely scrutinized the bureau rate filing. It required the bureau to file substantial supporting information with the requested rate increase. (*Ferraro* 2314, J.A. 59.) The bureau complied. (CX 30A to 30Z-97.) The filing included an explanatory letter (CX 30A-30B, J.A. 91-93), a lengthy A.D. Little profitability analysis (Pet. App. 192a; CX 30C to 30Z-79; RX 499; *Plotkin* 2629), the bureau's calculation of its projected rate of return based on the proposed rate increase (CX 30Z-80 to 30Z-81), and a marked-up rate manual reflecting the proposed increase in rates. (CX 30Z-82 to 30Z-97.)

The responsible Connecticut regulators reviewed all of the materials submitted by the bureau in support of its 1981 filing, described by one of them as "well supported and detailed." (*DiSanto* 2742, J.A. 77.) They discussed the filing, compared the rates proposed to previous filings and ultimately concluded that the filing satisfied statutory requirements. (*DiSanto* 2743-47, J.A. 77-79; *Bell* 2827-29, J.A. 83-84.) The department approved the filing. (Pet. App. 195a.)

In addition to these two comprehensive filings, the bureau filed amendments and endorsements from 1966 to 1983. As to these, the ALJ found that "apparently some were carefully reviewed while others were approved with minimal review; there was no showing, however, in the record that even this minimal review was inadequate considering the subject matter of these minor ancillary filings." (Pet. App. 191a, n.192.) The regulator testified that the department "reviews every filing that we receive" (*DiSanto* 2758, J.A. 80), and the uncontradicted evidence demonstrates that at least three of the endorsement filings were revised, withdrawn or disapproved after state insurance officials questioned certain features of those filings. (*DiSanto* 2759-69.)

All Respondents had withdrawn from the Connecticut bureau by the beginning of 1985, and the bureau ceased functioning in the first quarter of that year. (Pet. App. 195a, 217a; *DiSanto* 2728.

(3) Montana. The Montana rating bureau obtained its license in July 1982, (CX 37), but was defunct by 1985. (Pet. App. 217a.) It made filings in February 1983 (CX 41A-41E, J.A. 94-99), and October 1984 (CX 43A to 43Z-25).

In the years preceding the formation of the rating bureau, the Montana insurance commissioner had become particularly involved with title insurance rating and profitability issues by virtue of his participation in a national task force which studied these issues.[18] The Montana insurance department also held a hearing in 1979 to consider the impact, if any, on title insurance rates of the "controlled business" phenomenon in the industry. (RX 492N; *Plotkin* 2714-17, J.A. 73.) Dr. Plotkin of A.D. Little testified at this hearing, which entailed scrutiny of the profitability of title insurers. (*Plotkin* 2717, J.A. 73.)

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[18] The insurance commissioner had been involved in a task force created by the National Association of Insurance Commissioners ("NAIC"). (RX 502Z-44—502Z-50; RX 502Z-53—502Z-58; RX 502Z-76—502Z-128.) The task force, which was formed in 1972 (RX 502Q-502S), surveyed insurance departments to identify concerns relating to title insurance regulation (RX 502Z-45—502Z-48). The 1979 survey identified rate making as one of several subjects warranting further study. (RX 502Z-54.) The task force also gave attention to the methods for determining whether a title insurance rate is excessive, inadequate or unfairly discriminatory. (RX 502Z-64—502Z-72.) In 1982, the task force completed its drafting of a model title insurance act, many aspects of which were adopted in the Montana Title Insurance Act, enacted in 1985. (RX 502Z-103—128; Mont. Code Ann. §§ 33-25-104 to 33-25-403.)

The Montana insurance department in 1980 had asked that "consideration [be given] to the organization of an advisory committee to provide this office with a profitability study on the business of title insurance in Montana." (RX 514, J.A. 164-65.) At that time, the department had expressed concern that individual insurers were filing rates that would threaten insurer solvency. *Id.* The department objected to a March 1980 rate filing by the Title Insurance Company of Minnesota on the ground that "[t]o decrease rates would . . . possibly jeopardize the financial security of your company." (RX 506.) The department also rejected an April 1980 Chicago Title filing, although it indicated a willingness to consider "additional information . . . which would assure us that this filing would not result in 'inadequate' rates." (RX 511.) The department rejected another Chicago Title filing two months later stating that "we have the administrative duty to protect the solvency of companies." (RX 513.) The department eventually withdrew its objection to the lower rates filed by Chicago Title but pointed out that if its "profits continue to decline, we will have no alternative but to request that you either increase rates or discontinue the sale of title insurance in our state." (RX 514, J.A. 164.)

The Montana rating bureau's filing of February 1983 was accompanied by a five page letter submitted in order to justify the rates pursuant to the state statutory criteria. (CX 41A-41E, J.A. 94-99.) The letter pointed out that rates then in use by most individual insurers in Montana were adopted in 1966, so that the use of such rates when "considered with the tremendous increase in operational costs caused by the inflationary trends of our economy," (CX 41E, J.A. 99), "makes the profitability of the Montana title insurance industry questionable," (CX 41B, J.A. 95). Further, the letter noted that nationally the title insurance industry had "lost $63.6 million in 1980, $110.3 million in 1981 and the figures for the first half of 1982 indicates [sic] an even poorer performance."

(CX 41B, J.A. 95.)[19] This letter also pointed out that in response to severe losses in the industry, most title insurance companies had "taken drastic steps to reduce expenses." (CX 41C, J.A. 97.) The letter stated that the rating bureau would submit a profitability study within the following year but that the solvency threat to the industry mandated prompt submission of the proposed rates for approval. (CX 41E, J.A. 99.)

A representative of the bureau personally delivered the rate filing and support letter to the commissioner on February 22, 1983. The commissioner escorted the bureau representative to the department official in charge of title insurance rate filings, who discussed the filing with the bureau representative: "We took a look at the filing, discussed the filing for a while, talked about its contents and discussed also what type of justification they would want as far as statistics." (*Statton* 2858, J.A. 88.) The regulator explained the format of the statistics that would be required by the department. (*Statton* 2859, J.A. 88.) According to the ALJ, the bureau "was told that while the increase would go into effect immediately, additional support would have to be provided." (Pet. App. 213a.) Although the statistical information was collected by the bureau (*Statton* 2859, 2868), before it could be submitted to the department most members had withdrawn. (*Statton* 2863, 2868.)

The bureau filing of October 18, 1984, (CX 43A-43Z-25), which was "basically a clarification of the 1983 filing plus an increase in the charges for special endorsements" (Pet. App. 213a n.267), precipitated a request from the department for supporting documentation (RX 227) which was submitted on December 18, 1984. (CX 44A-44E.) Although the department approved the filing to be effective January 2, 1985, (CX 45), apparently only two members remained in the bureau at that time. (*Statton* 2858.)

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[19] The department had earlier requested national data in support of individual filings. (RX 508).

Respondents resigned from the Montana bureau over the period from July 1983 to January 1985, and the bureau had ceased to function by January 1985. (Pet. App. 214a, 217a.)

(4) Wisconsin. The Wisconsin rating bureau submitted general rate filings in 1971, 1981 and 1982, as well as various endorsement filings.

The Wisconsin bureau was formed in 1969 with the encouragement of the insurance department. (*Donahoe* 1615-16, J.A. 2; CX 107.) At a meeting of the bureau and insurance department personnel prior to its initial filing (*Donahoe* 1619-20; J.A. 2-3; RX 302, J.A. 130-31), the department "indicated that [it] would carefully review [the] filing when formally made," (RX 302, J.A. 2-3). Bureau personnel explained to the department that the rate filing would be based upon "historical rates." (Pet. App. 198a; *Donahoe* 1618, 1620, J.A. 2-3.) Because the industry had no composite statistical data reflecting the newly filed rates, the department indicated that the "filing would be accepted subject to the subsequent filing of rate justification statistics" demonstrating the composite experience of the industry under the filed rates. (*Donahoe* 1619-20, J.A. 3.)

The department responded to the 1971 filing by indicating that the rates were acceptable but requesting an explanation for the fact that search and examination charges were filed only for certain southeastern counties in Wisconsin. (RX 303, J.A. 132-33; *Donahoe* 1623, 1625.) The department subsequently rejected the bureau's explanation (*Donahoe* 1626), and the rate bureau in 1974 submitted an amended filing extending the geographic scope of the search and examination charges (RX 312), which was approved (Pet. App. 198a).

Beginning prior to the approval of the initial filing and continuing over the next several years, bureau and insurance department officials discussed the development of rate justification materials and other matters. Department and bureau personnel met in July 1973 (RX 305, J.A. 134; RX 306; RX 307, J.A. 135), and again in March and July 1974 (RX 309-09A; RX 316, J.A. 139). In February and April 1975, the department held hearings that dealt with rate justification and other title insurance issues. (RX 320-320E; *Plotkin* 2585-86, J.A. 65.) In August 1976 a department rate analyst, based on information that had been supplied at the 1975 hearings and later information, concluded that the industry "appear[ed] to be following the depressed earnings cycle of the property liability business fairly closely" and "suggested that we take another look at this when the 76 results are in to see if there has been any improvement in the earnings of this industry." (RX 335, J.A. 148.)

A proposed data collection system designed for the bureau by the A.D. Little consulting firm was submitted in August 1976. (RX 334 to 334Z-19; *Plotkin* 2587-88, J.A. 66.) Bureau and department personnel met in September 1976 to discuss the data collection system, (RX 336-336B, RX 340), and the plans were officially submitted to the department in November 1976 (RX 340), and were reviewed and approved by it. (RX 341, J.A. 150-51.)

In February 1981 the bureau submitted its first general rate adjustment. (*Donahoe* 1645-46; *Grabski* 1703-04; *Wirtz* 1811.) At a meeting with a bureau representative before the filing, a department representative was "adamant" that any rate increase would have to be justified "because the department was not about to okay increases in rates just offhand." (*Grabski* 1704, J.A. 8.) When the rate filing was received, the department rate analyst "discussed it with [his] supervisor" and stated that "it would be wise for us to look at it closely." (*Wirtz* 1750, J.A. 16.) Because the filing proposed a rate increase of approximately eleven percent (*Wirtz* 1751, J.A. 16), the department told the bureau that it "could very well" hold a hearing on the matter unless sufficient justification was submitted (*Grabski* 1707-08, J.A. 9-10). The department advised the bureau by letter in April

1981, that the filing was "in the process of being reviewed" and that "there may be a need to request further documentation regarding the rate change." (RX 367, J.A. 152.) The rate analyst continued his review of the filing as follows:

> I put on my actuarial hat and, first of all, took all the information that was in the filing and checked its mathematical accuracy. In addition to that, I pulled out the Plotkin studies to use what was relevant in that and checked it against the numbers in the filing.
>
> In addition to that, I pulled out all the annual statements for the title companies and I added together the numbers of those companies involved in the rate filing. And I also checked that against the accuracy of the rates in the rate filing, the accuracy of the data in the rate filing. And then I adjusted the rates at different levels to see how different rate increases would [affect] residential versus commercial and played with different kinds of rates and so forth.

(*Wirtz* 1752, J.A. 17.) He continued his review by making a rate comparison with rates in effect in Minnesota and Illinois. (*Wirtz* 1825, J.A. 20.)

Bureau and department personnel met in May 1981 to discuss the filing. The primary concern of the department representatives was the adequacy of the justification submitted for the rate increases. After the meeting the bureau supplied additional statistical material. (RX 369-369A, J.A. 153-54; RX 370-370Z-17, J.A. 155-62; *Grabski* 1710-11, J.A. 10-11.) A similar meeting was held in late July 1981 (RX 371; *Grabski* 1713, J.A. 11-12), at which time the "Commissioner was '95%' convinced that [the] filings were acceptable," (RX 371). Although the rate analyst thought there were "grounds to attack" the filing and there were some "weaknesses in it," he "went through a weighing and judgmental process" and "came to the conclusion that it was justified." (*Wirtz* 1824-25). He testified that he "looked at

the submission by the rating bureau very carefully because it was a substantial one" (*Wirtz* 1824), and that we "gave the 1981 filing an intensive review" (*Wirtz* 1799, J.A. 20). Thereafter he informed the president of the bureau that the department accepted the 1981 filing. (*Grabski* 1714, J.A. 12.) The Commission concluded, without record citations, that the 1981 filing was checked "merely for mathematical accuracy." (Pet. App. 63a.)

The Wisconsin bureau submitted its third and final general rate filing in October 1982. (RX 374; *Grabski* 1715, J.A. 13.) Before the filing was submitted, the president of the rating bureau had had "three or four discussions" with the rate analyst "explaining to him what direction we were going in." (*Grabski* 1715, J.A. 13.) The rate analyst stated "that if you are talking about rate increases, you better be prepared to justify them." (*Grabski* 1715, J.A. 13.) The rate filing was accompanied by an A.D. Little analysis which concluded "that the proposed rates result in an annual pro forma overall rate of return on total capital of 5.94%" while the rate of return from the existing rates would be 0.09%. (RX 375B-375C; RX 374A.) According to Dr. Plotkin, this information made it "obvious" that the proposed rates were not excessive. (*Plotkin* 2604-05.) The rate analyst "reviewed the filing" (*Wirtz* 1757, J.A. 18; RX 377, J.A. 163), and requested a replacement copy of the A.D. Little financial report for the years 1972-1981, which was supplied by the rating bureau (RX 377, J.A. 163). Thereafter, the department accepted the filing. (RX 378.)

In addition to its three general rate filings, the bureau from time to time made endorsement filings, some of which specified a rate for the endorsement coverage. The record shows scrutiny of the coverage provided by these forms (*e.g.*, RX 314, RX 315, RX 342, RX 343-343B; *Grabski* 1695; *Wirtz* 1760; RX 373, RX 380-380A), some severe questioning of particular coverage, (*e.g.*, regarding a proposed zoning endorsement, the department

asked: "How can a zoning classification of property be categorized as an encumbrance or defect in title?" RX 315), and occasional rejection of proposed endorsements (*e.g.*, RX 373D). As to proposed rates for certain endosements, the rate analyst testified that "we would look at them and apply some kind of a judgment sense as to whether they were too high or too low." (*Wirtz* 1769, J.A. 18.) The department was apparently unsure what information could be generated that would scientifically "justify" any particular endorsement rate. (*Wirtz* 1808.) (The rate analyst testified that "[j]udgment rating is a very common element in rating." *Wirtz* 1808.) In addition, the Wisconsin department chose to devote fewer resources to the review of rates for endorsement filings because experience had shown that these rates were kept in check by competition among title insurance companies through the filing of "deviation" rates. (*Wirtz* 1804-05.)

The Wisconsin bureau was dissolved effective December 31, 1984. (Pet. App. 200a.)

SUMMARY OF ARGUMENT

The Federal Trade Commission challenged the state regulatory programs at issue here by singling out particular regulatory actions that, in its view, could have been done better. The Third Circuit correctly held that this qualitative assessment cannot be squared with the teachings of this Court and basic principles of federalism.

The state action doctrine holds that state anticompetitive activity is not subject to federal antitrust law, because of the special status of States as sovereigns within the federal system. *City of Columbia v. Omni Outdoor Advertising, Inc.*, 111 S.Ct. 1344, 1351 (1991) (*"City of Columbia"*). In state action analysis, a State's active superviison serves "essentially an evidentiary function." *Town of Hallie v. City of Eau Claire*, 471 U.S. 34, 46 (1985) (*"Hallie"*). Active supervision is proof that the State's anticompetitive program is a legitimate one that

seeks to have private actors conform to the State's policies, and is not merely an attempt by the State to immunize private actors from antitrust liability. *Id.*; *Midcal*, 445 U.S. at 106. To serve this evidentiary function without intruding unnecessarily on state sovereignty, the active supervision inquiry focuses on whether a legitimate regulatory program exists—a program, that is, in which "state officials have and exercise power" to review anticompetitive activities. *Patrick*, 486 U.S. at 100-01.

The active supervision standard used by the Third Circuit Court of Appeals below is adopted from a decision of the First Circuit which also rejected the Commission's approach. *New England Motor Rate Bureau Inc. v. F.T.C.*, 908 F.2d 1064 (1st Cir. 1990) (*"New England"*). The standard strikes a careful balance between federal antitrust goals and the federalism concerns underlying the state action doctrine. It recognizes that state statutory systems are strong evidence of active supervision when they provide officials with both the legal authority and the duty to regulate according to established regulatory standards. Further evidence may be found, as the Third Circuit concluded, in the fact that a program is "in place, staffed and funded," and shows "some basic level of activity directed toward seeing that the private actors carry out the state's policy and not simply their own policy." (Pet. App. 28a, *quoting New England*, 908 F.2d at 1071.) In the States here there was abundant evidence of legitimate regulatory programs, both in the statutes and in regulatory activity.

The Commission's approach, in contrast, intrudes into state regulatory decisions in order to further federal antitrust policy objectives. The Commission did not limit itself to determining that regulatory programs existed but substituted its own judgment concerning the quality of state regulation. The Third Circuit correctly held that the FTC was in error because "[t]he principles of federalism and state sovereignty that undergird the doctrine prohibit its selective application only where states act in

a manner that a federal agency or a federal court finds to be preferable." (Pet. App. 37a.)

If such intrusive second-guessing is permitted as part of active supervision analysis, the resulting unpredictability would substantially diminish the flexibility of the States to regulate. State programs requiring private cooperation could not function if cooperation exposed the participants to the threat of antitrust liability. In short, the Commission's approach to active supervision ignores the evidentiary function of the requirement and is contrary to the federalism principles underlying the state action doctrine.

ARGUMENT

I. THE ACTIVE SUPERVISION REQUIREMENT WAS DESIGNED TO ASSURE THAT THE STATE ACTION DOCTRINE APPLIES ONLY WHERE THE STATE HAS ESTABLISHED A PROGRAM OF SUPERVISION TO IMPLEMENT ITS REGULATORY POLICIES.

As the Court has observed, "[t]he starting point in any analysis involving the state-action doctrine is the reasoning of *Parker v. Brown*, [317 U.S. 341 (1943) (*"Parker"*)]." *Hoover v. Ronwin*, 466 U.S. 558, 567 (1984) (*"Hoover"*); *Hallie*, 471 U.S. at 38. In *Parker*, relying upon principles of federalism and state sovereignty, this Court held that the federal antitrust laws were not intended "to restrain state action or official action directed by a state." 317 U.S. at 351.

In decisions since *Parker*, this Court repeatedly has invoked this federalism theme and has articulated a state action test that recognizes "the States' freedom to engage in anticompetitive regulation." *City of Columbia*, at 1353. The most comprehensive enunciation of this theme is found in *Southern Motor Carriers Rate Conference, Inc. v. United States*, 471 U.S. 48, 50 (1985) (*"Southern Motor Carriers"*), where the Court applied the state action doctrine to the same kind of activity as is involved

in this case, *i.e.*, tariff filings by rating bureaus. The Court rejected a reading of state action that would have required that States compel rating bureau membership, on grounds that a "compulsion requirement is inconsistent" with the "principles of federalism and the goal of the antitrust laws" because "[i]t reduces the range of regulatory alternatives available to the State." *Id.* at 61. In doing so, the Court affirmed that "[t]he *Parker* decision was premised on the assumption that Congress, in enacting the Sherman Act, did not intend to compromise the States' ability to regulate their domestic commerce." *Id.* at 56.

Because federalism principles lie at the core of the state action doctrine, the doctrine does not place substantive limits on state regulation. When, as here, a State's anticompetitive program is "clearly articulated and affirmatively expressed as state policy," the only additional requirement for state action is that the activity conducted pursuant to that policy be " 'actively supervised' by the State itself." *Midcal*, 445 U.S. at 105 (citation omitted).

As this Court has explained, the active supervision requirement "serves essentially an evidentiary function." *Hallie*, 471 U.S. at 46. It addresses the risk that a state might attempt to "give immunity to those who violate the Sherman Act by authorizing them to violate it, or by declaring that their action is lawful." *Midcal*, 445 U.S. at 106 (*quoting Parker v. Brown*, 317 U.S. at 351). *See also Patrick*, 486 U.S. at 100-01; *324 Liquor Corp. v. Duffy*, 479 U.S. 335, 345 (1987) (*"324 Liquor"*). The active supervision requirement ensures that a State has not clearly articulated an anticompetitive policy merely to thwart federal law with "a gauzy cloak of state involvement." *Midcal*, 445 U.S. at 106. Active supervision serves as proof that when a State has authorized an anticompetitive program, the program serves "the governmental interests of the State," rather than purely private interests. *Hallie*, 471 U.S. at 47. *See also Pat-*

rick, 486 U.S. at 100-01; Merrick B. Garland, *Antitrust and State Action: Economic Efficiency and the Political Process*, 96 Yale L.J. 486, 501 (1987).

This Court has applied the active supervision requirement articulated in *Midcal* in only three cases: *Midcal*, *324 Liquor* and *Patrick*. In *Patrick*, the Court said that active supervision "requires that state officials have and exercise power to review particular anticompetitive acts of private parties and disapprove those that fail to accord with state policy." 486 U.S. at 101. However, these cases all involved States which had authorized private anticompetitive conduct yet failed to establish a regulatory system for the supervision of that conduct. Thus, the Court has not directly addressed the application of the active supervision requirement in a case such as this one, in which States have provided by legislation for regulatory supervision and state regulators have reviewed private conduct.

To be consistent with the principles of federalism and state sovereignty underlying the state action doctrine, the requirement of active supervision should not be interpreted so as to require state regulation to conform to a particular design. *See Patrick*, 486 U.S. at 101-05; *Midcal*, 445 U.S. at 105-06. *See also Southern Motor Carriers*, 471 U.S. at 61 (interpreting state action so as to avoid "reduc[ing] the range of regulatory alternatives available to the State"). The active supervision requirement should be satisfied by the *existence* of a regulatory program. As long as a State has clearly articulated its intent to replace competition with regulation and has established a regulatory program, there is assurance that the State is not merely authorizing antitrust violations.

The *quality* of a State's regulatory program should have no bearing on active supervision analysis. The quality of a state regulator's work is, of course, a matter of concern to the State seeking to fulfill its policy objectives. But once the existence of a regulatory program is established, it would serve no purpose to involve federal antitrust tribunals in policing the effectiveness of state programs designed to serve public policies that may conflict with federal antitrust goals. Indeed, if federal antitrust tribunals were permitted to overrule the States' determinations on how best to achieve their policies, "the state action doctrine would be turned on its head." *New England*, 908 F.2d at 1071. *See City of Columbia*, 111 S.Ct. at 1350 (rejecting interpretation of state action that would transform "state administrative review into a federal antitrust job," *quoting* Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* § 212.3b, at 145 (Supp. 1989)).[20]

The design and implementation of a regulatory program, as well as particular regulatory decisions, depend largely upon policy judgments, such as how best to allocate state resources and how to balance a variety of state policy goals. Such judgments are traditionally matters of state prerogative. As this Court observed in *Hoover*, 466 U.S. at 574, the issue is not whether "the sovereign [has] acted wisely" but simply whether "the state [has acted] as sovereign." *Accord*, *Llewellyn v. Crothers*, 765 F.2d 769, 774 (9th Cir. 1985) (Kennedy, J.) ("A state's antitrust immunity springs from an essential principle of federalism, the necessity to respect a sovereign capacity in the several states. . . . Given this purpose, it follows that actions otherwise immune should not forfeit that protection merely because the state's at-

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[20] Professor Milton Handler has stated:

> What would be inconsistent with *Parker* would be an inquiry into the effectiveness of the state's supervision, for then the federal courts would be making subjective judgments about the adequacy and not merely the actuality of state regulation—the kind of second-guessing which . . . runs directly counter to the principle of federalism upon which *Parker* rests.

Milton Handler, *Antitrust 1978*, 78 Colum. L. Rev. 1363, 1386-87 (1978).

tempted exercise of its power is imperfect in execution under its own law." (citation omitted)).[21]

Moreover, post hoc judgments as to the quality or effectiveness of state regulatory determinations will lack predictability and for this reason will undermine state regulatory programs. State programs such as those here are possible only if private parties participate. *See Southern Motor Carriers*, 471 U.S. at 58. If participation involves a substantial risk of antitrust liability—that is, if the quality or effectiveness of the States' regulatory determinations may be subject to later federal antitrust review—the programs will fail for lack of participation.[22] Such a review cannot be part of the active

[21] *See also, e.g.*, Einer Richard Elhauge, *The Scope of Antitrust Process*, 104 Harv. L. Rev. 668, 692 (1991) ("State administrative law, not antitrust review, is the proper remedy for preventing state agencies from exceeding or abusing their authority. States can always provide further remedies if they find them necessary."); Phillip E. Areeda, *Antitrust Immunity For "State Action" After Lafayette*, 95 Harv. L. Rev. 435, 453 (1981) (" 'Ordinary' errors or abuses in the administration of powers conferred by the state should be left for state tribunals to control.").

[22] In this case, the pendency of the FTC's investigation caused so many title insurers to withdraw from rating bureau participation that by the time the FTC filed its complaint in January 1985, all the existing title insurance rating bureaus in the country had effectively ceased to function. The title insurers' antitrust liability concerns were not fanciful. Beginning within hours after the FTC filed its complaint, the Respondents became defendants in a series of more than a dozen private treble damage class actions. *See In re Real Estate Title and Settlement Services Antitrust Litigation*, 1986-1 Trade Cas. (CCH) ¶ 67,149 (E.D.Pa. 1986), *aff'd mem.* 815 F.2d 695 (3d Cir. 1987), *cert. denied*, 485 U.S. 909 (1988). Though these class actions were settled, *id.*, later cases continued to be filed arising out of the same matters as the FTC case, two of which are still pending. *Brown v. Ticor Title Ins. Co.*, No. CIV-90-0577 PHX SMM (D. Ariz., summary judgment granted March 5, 1991), *app. pending*, No. 91-15474 (9th Cir.); *Prentice v. Title Ins. Co. of Minnesota*, No. 89-CV-012004 (Circuit Ct., Milwaukee Cty., Wis., dismissed Jan. 18, 1991), *app. pending*, Docket No. 91-1580 (Wis. Ct. App.).

supervision analysis, since it would subvert, rather than implement, the state action doctrine. *Cf. City of Columbia*, 111 S.Ct. at 1351 (rejecting conspiracy exception because it "would virtually swallow up the *Parker* rule").

The active supervision requirement must be applied with a view to its evidentiary purpose and federalism principles. Applied this way, the inquiry here should be straightforward. The legitimacy of the type of program at issue here is not subject to reasonable dispute. This Court in *Southern Motor Carriers* acknowledged the usefulness of collective rate filing through rating bureaus as part of a system of state regulation. 471 U.S. at 51. The state programs in this case were not ones in which the States merely authorized private anticompetitive conduct. The States enacted comprehensive regulatory programs with staffed and funded agencies charged with assuring that the States' rate policies were adhered to. Over the period encompassed by this proceeding, regulators gave administrative attention to these bureaus and their rate filings. Such regulatory programs amply satisfy the goals of the active supervision requirement, as the Third Circuit held.

II. THE THIRD CIRCUIT FAITHFULLY APPLIED THIS COURT'S STATE ACTION PRECEDENT IN REVERSING THE DECISION OF THE FEDERAL TRADE COMMISSION.

1. The Third Circuit applied a standard of active supervision articulated by the First Circuit in the *New England* case:

> Where . . . the state's program is in place, is staffed and funded, grants to the state officials ample power and the duty to regulate pursuant to declared standards of state policy, is enforceable in the state's courts, and demonstrate some basic level of activity directed towards seeing that the private actors carry out the state's policy and not simply their own policy, more need not be established.

(Pet. App. 28a, *quoting New England*, 908 F.2d at 1071.)

This standard is not a "toothless" legal standard that does away with the active supervision requirement. FTC Brief at 22. Nor is it true that these Circuits "did not purport to derive [their] legal standard from any decision of this Court." *Id.* at 21. On the contrary, the standard applied by both Circuits respects the principles of state sovereignty and federalism underlying the state action doctrine, and follows this Court's directive to apply the active supervision requirement by focusing on whether the State "ha[s] and exercise[s] power to review" the private acts at issue for conformance to state policy. *Patrick*, 486 U.S. at 101.

In assessing whether the State "has" regulatory power, these Circuits asked whether the state agency had the legal authority to review and disapprove filed rates for failure to conform to substantive state regulatory criteria. (Pet. App. 28a.) This initial focus of the Circuit Courts' test is consistent with the body of cases in this Court and others that have determined whether a regulatory program exists by inquiring whether state statutes grant authority for substantive review of regulated conduct. *E.g. Patrick*, 486 U.S. at 102 (no active supervision where state statutory scheme did not empower state regulators or courts to engage in substantive review of the regulated conduct); *324 Liquor*, 479 U.S. at 335-36 (no active supervision where state statutes did not give regulators authority to approve or disapprove privately set price schedules, because "[t]he State has displaced competition among liquor retailers without substituting an adequate system of regulation"); *Midcal*, 445 U.S. at 106 (statutory scheme that did not empower state regulators to review the reasonableness of filed price schedules did not satisfy active supervision requirement); *New Motor Vehicle Board of California v. Orrin W. Fox Co.*, 439 U.S. 96 (1978) (state action doctrine applied on the basis of a review of the statutory provisions at issue). Indeed, no decision of this Court has ever found an absence of active supervision where there was state authority to engage in substantive review of the regulated private conduct.[23]

Lower federal courts have found active supervision on the basis of the existence of a statutory system of regulation. For example, in *Capital Telephone Co. v. New York Telephone Co.*, 750 F.2d 1154, 1163-64 (2d Cir. 1984), *cert. denied*, 471 U.S. 1101 (1985), the Second Circuit determined that active supervision existed by finding that "the state legislature had 'expressly conferred' powers upon the [Public Service Commission] which enabled it to review rates and other aspects of telephone company operations for reasonableness." *Id.* at 1163. After reviewing the New York statutory program, the court concluded:

> It would be inconsistent with such a broad regulatory scheme to find that the particular activities in question are subject to antitrust liability where the legislature so clearly intended to allow the PSC to control all activities which are a reasonable part of such a regulatory scheme. Therefore, we agree with the district court that this regulatory program constitutes "active supervision" under *Midcal*.

Id. at 1164.[24]

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[23] In fact, the "have and exercise" language of *Patrick* had its genesis in this Court's review of the *statutory* schemes of regulation in *Southern Motor Carriers*:

> Common carriers are required to submit proposed rates to the relevant commission for approval. A proposed rate becomes effective if the state agency takes no action within a specified period of time. If a hearing is scheduled, however, a rate will become effective only after affirmative agency approval. The State Public Service Commissions thus *have and exercise ultimate authority and control over all intrastate rates.*

471 U.S. at 50-51 (emphasis added, footnotes omitted).

[24] *See also, Llewellyn v. Crothers*, 765 F.2d 769, 773 (9th Cir. 1985); *Marrese v. Interqual, Inc.*, 748 F.2d 373, 390-91 (7th Cir.

However, the Circuit Court standard applied here goes beyond inquiring whether the State "has" power to regulate pursuant to the statutory system of regulation. It also requires evidence demonstrating that the State in fact "exercised" its powers of review under that system. The standard looks to the terms of the statutes themselves for evidence that state officials are granted not only "ample power" but also the "duty" to regulate, and that the program is "enforceable in the state's courts." (Pet. App. 28a.) In addition, the Circuit Court standard demands a showing that in fact the regulatory program is "in place, staffed and funded," and that there is "some basic level of activity directed towards seeing that the private actors carry out the state's policy and not simply their own policy." *Id.*

The reasoning underlying this approach begins with the recognition that the very existence of a statutory program of regulation provides evidence that state regulatory control is actually being exercised. This conclusion results from provisions of state law that affirmatively impose on state officials regulatory duties—"duties which a federal court may not, under normal principles of federalism, assume [state officials] will disregard." *New England*, 908 F.2d at 1072.[25] To assure that these

1984), *cert. denied*, 472 U.S. 1027 (1985); *Euster v. Eagle Downs Racing Association*, 677 F.2d 992 (3d Cir.), *cert. denied*, 459 U.S. 1022 (1982); *Turf Paradise, Inc. v. Arizona Downs*, 670 F.2d 813, 824-25 (9th Cir.), *cert. denied*, 456 U.S. 1011 (1982); *Morgan v. Division of Liquor Control*, 664 F.2d 353, 356 (2d Cir. 1981); *Monarch Entertainment Bureau, Inc. v. New Jersey Highway Authority*, 715 F. Supp. 1290, 1298 (D.N.J.), *aff'd*, 893 F.2d 1331 (3d Cir. 1989); *Capital Telephone Co., Inc. v. City of Schenectady*, 560 F. Supp. 207, 210-211 (N.D.N.Y. 1983); *Fisher Foods, Inc. v. Ohio Dept. of Liquor Control*, 555 F. Supp. 641, 647 (N.D. Ohio 1982).

[25] The presumption of regularity attaching to official conduct is recognized in precedent in this Court and in each of the states at issue. *E.g. U.S. v. Chemical Foundation*, 272 U.S. 1, 14-15 (1926) ("The presumption of regularity supports the official acts of public officers, and, in the absence of clear evidence to the contrary, courts

duties are not "mere precatory maxims," the standard further inquires whether the regulatory duties imposed on state officials are "enforceable by mandamus and other legal remedies in state courts." *Id.* at 1072 n.10.

The Circuit Court standard seeks further confirmation of the exercise of state regulatory power by requiring evidence that the program is "in place, staffed and funded," and of "some basic level of activity directed towards seeing that the private actors carry out the State's policy and not simply their own policy." (Pet. App. 28a, *quoting New England*, 908 F.2d at 1071.)[26] This formulation reflects a careful balancing of the inherent tension between the federalism principles underlying the state action doctrine and the evidentiary purpose of the active supervision requirement. By inquiring into the *existence* of state regulatory activity "directed towards seeing that the private actors carry out the state's policy," the Court of Appeals standard embodies precisely the purpose of the active supervision requirement as articulated by this Court in *Hallie*—the "essentially . . . evidentiary function" of "ensuring that the actor is engaging in the challenged conduct pursuant to

presume that they have properly discharged their official duties.") *Thompson v. Consolidated Gas Utilities Corp.*, 300 U.S. 55 (1937); *Ross v. Reed*, 14 U.S. (1 Wheat.) 482, 486 (1816); *Berry v. Merchants Life & Cas. Co.*, 195 N.W. 335, 336, 181 Wis. 487 (1923); *Trustees, Missoula County School Dist. 1 v. Anderson*, 757 P.2d 1315 (Mont. 1988); *Cagle v. Home Ins. Co.*, 14 Ariz. App. 360, 483 P.2d 592, 598 (1971); *Bowman v. 1477 Central Ave. Apartments*, 203 Conn. 246, 524 A.2d 610, 615 (1987).

[26] Contrary to the FTC's contention, the Circuit Court standard would *not* permit a finding of active supervision based on a record showing nothing more than "inaction or passive acquiescence" by the State with respect to the private conduct. FTC Br. at 20. By its express terms, the standard requires that the States act not only to establish a regulatory program with the specified powers, duties and substantive criteria, but also to staff and fund the program, and that there be evidence of "activity" directed toward seeing that private actions conform to state policies.

state policy." *Id.* at 46. At the same time, by carefully avoiding an evaluation of the *quality* or the *effectiveness* of the State's activity, the Circuit Court formulation embodies the respect for state regulatory autonomy that is the heart of the state action doctrine itself. The question it asks is the proper one: Having established a system to regulate according to substantive state policies, is the State taking steps—engaging in a "basic level of activity"—to see that its policies are followed? The choice of supervisory activities is left to the State, whose policies and program are its own.

The Third Circuit correctly found that the facts in the administrative record established "active supervision" under the appropriate legal standard in each of the four States. In each State, the court looked first to the statutory provisions under which the regulatory program was administered, and found that the statutes gave the insurance departments both the power and the duty to regulate the filed rates under declared standards of state policy. (Pet. App. 30a-31a, 33a, 35a, 36a.) It found that the duty to regulate was enforceable in the State's courts. *Id.* Assessing the administrative record, it found that the program of supervision in each State was "in place, staffed and funded" during the period at issue, and that in each State the insurance department demonstrated activity directed toward seeing that the regulated title insurers carried out the State's rate policies. (Pet. App. 31a, 33a, 35a, 36a-37a.) On the latter point, the Third Circuit eschewed the Commission's approach of criticizing the *quality* of state activity, finding the *existence* of supervisory activity in record evidence that state regulators review rate filings, sought additional information from regulated parties, established policies to examine rate filings, and approved certain rates. *Id.*[27] As the dis-

[27] The Commission argues that the Third Circuit erred by citing evidence of state regulatory approvals which in the FTC's view pertained only to the form of a rate filing, and not to conformance with substantive rate criteria. (FTC Br. 23-24 n.16, 29, 30). The Commission cites no record support for its distinction, which was never referred to in its decision below. Moreover, the state statutes when using the language of "approval," "disapproval" or similar terms, consistently refer to substantive issues and make no provision for approval as to form. E.g., Ariz. Rev. Stat. Ann. §§ 20-376(D), 20-378 (J.A. 168, 170-71); Conn. Gen. Stat. Ann. §§ 38-201n(c), 38-201x(a)(2), -(b)(2) and -(b)(4) (J.A. 177, 184-85, 186, 187); Mont. Code Ann. § 33-16-205 (J.A. 196); Wis. Stat. Ann. §§ 625.13(2), 625.22 (J.A. 207, 208-09). The distinction appears to be another way for the FTC to inquire into the quality and merits of state regulatory decisions, in contrast to the Third Circuit's approach of ascertaining the existence of state activity directed towards seeing that state law requirements were carried out.

cussion earlier in this brief indicates, the Third Circuit's conclusion is amply supported by the substantial record evidence of regulatory activity.

Any test of active supervision which involves an evaluation of the actual activities of state regulators risks, as the ALJ said, "laps[ing] over into a qualitative evaluation of the performance of state officials." (Pet. App. 239a.)[28] However, the First and Third Circuits' careful approach permits a focused but deferential inspection of actual state supervision, leaving to the States themselves rather than federal antitrust authorities the details of enforcing state regulatory programs. It comports fully with this Court's statements of the scope and purpose of the active supervision requirement, and the federalism principles on which the state action doctrine is based.[29]

[28] Federal courts should not "scrutinize the rigor with which the state supervises the challenged activity to ensure that supervision is more than pro forma" because "[t]here simply is no way to tell if the state has 'looked' hard enough at the data." 1 Phillip E. Areeda & Donald F. Turner, *Antitrust Law* ¶ 213c, at 75 (1978).

[29] The state action doctrine applies to private conduct not because the private conduct is transformed into the action of the State, but because a failure to apply the state action doctrine to private conduct would frustrate the ability of States to implement regulatory programs. *Southern Motor Carriers*, 471 U.S. at 56. Thus the antitrust state action doctrine differs fundamentally from the concept of "state action" used to determine the scope of liability for claims

2. The flexibility permitted States under the Circuit Court standard is not acceptable to the FTC. Instead, the Commission proposes a more restrictive version of the test in *Patrick*, which requires that state officials "have and exercise power to review particular anticompetitive acts of private parties and disapprove those that fail to accord with state policy." 486 U.S. at 101. The *Patrick* standard requires the cop to be on the beat. But the Commision finds the active supervision requirement satisfied only where there is "an affirmative determination by state officials that the particular activity at issue is consistent with state policy." (FTC Br. at 20.) The FTC standard finds active supervision only where the cop catches every miscreant and awards a gold star to every law abiding citizen.[30]

The Commission's reformulation of *Patrick* would work to "reduce[] the range of regulatory alternatives available to the State" as clearly as the compulsion test rejected in *Southern Motor Carriers*, 471 U.S. at 61. The choice of the procedures to implement its regulatory programs is a matter for the State to decide. Visible, affirmative determinations, in advance, by state officials that planned private conduct comports with state policy (which the FTC demands) may be one way of assuring that the State has exercised its power to review. But in

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of deprivation of constitutional rights under 42 U.S.C. § 1983, referred to at FTC Br. 20 n.12. There is no reason to equate the antitrust doctrine's interest in furthering private parties' conformance to state regulatory policies with the § 1983 mechanism, which is intended to frustrate state actions that infringe on constitutional rights.

[30] This Court's formulation of the active supervision requirement in *Patrick* contemplates that state officials have and exercise the power to "review" private anticompetitive acts and to "disapprove" those that do not comport with state policy. 486 U.S. at 101. Nowhere is it stated that the state officials must act "affirmatively to review and approve" the private acts, as the Commission contends. (Pet. App. 55a.)

the real world it is certainly not the only way, and may not be the best way, to ensure that the State's policies are followed on an ongoing basis.

It may be entirely reasonable, for example, for a state regulator to achieve compliance with state policies in precisely the opposite fashion—by withholding approval of certain private conduct but placing the regulated parties on notice of its powers to act against them if their conduct should fail to conform to regulatory standards. Similarly, many States have chosen to adopt procedures by which proposed action is deemed approved if it is not rejected by state officials. These "deemer" or "negative option" procedures are designed to provide regulators the opportunity to allow proposed action to become effective without affirmative approval.[31] When a regulator reviews filings and allows them to become effective there is no reason to assume that the regulator is not actively supervising. A regulator interested in results rather than empty formalities may find that she can achieve compliance by regulated parties with state policy most effectively by allocating the State's resources to particular private conduct that the State deems most important.[32]

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[31] By statute, proposed rates in the four States at issue were effective if the state agency took no affirmative action to challenge the filed rate. However, the Commission's reliance upon these statutes (FTC Br. at 3, n.2) ignores the ALJ's finding that in actual practice the bureaus in Arizona and Wisconsin did not implement major rate charges until after the filings were formally stamped as approved by the department. (Pet. App. 197a, 201a.) The record demonstrates that the same was true in Connecticut and Montana. (Pet. App. 191-2a, 195a, 213a.)

[32] Commissioner Azcuenaga, dissenting in part from the Commission's opinion in *New England*, commented upon the impact of the Commission's standard upon negative option procedures:

> If use of negative option procedures is insufficient supervision for purposes of the state action doctrine, then the state will be forced to make a show of exercising its discretion to keep the [Federal Trade] Commission from interfering with the imple-

The Circuit Court standard recognizes that evaluating the legitimacy and effectiveness of such regulatory choices is beyond the proper scope of federal court review under the state action doctrine. By limiting its review of actual regulatory conduct to whether there is "some basic level of activity directed toward seeing that the private actors carry out the state's policy," this standard reflects the limited role that federal courts may properly play in reviewing the administrative activities of States.[33]

3. The Commission fundamentally distorts the Circuit Court standard by arguing that the standard is satisfied by the "mere availability of a state judicial remedy."

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mentation of its regulatory policy. This in turn would reduce the state's discretion in a manner probably inconsistent with the state action doctrine.

In the Matter of New England Motor Rate Bureau, Inc., 1989 FTC LEXIS 62, *67 n.9 (Docket No. 9170, 1989).

[33] The FTC Amici claim that the active supervision standard adopted by the Third and First Circuits would undercut the States' ability to implement narrowly-tailored regulatory schemes, such as New Jersey's law prohibiting insurers from using rating organizations for any purpose other than pooling loss data. FTC Amici at 16. This claim is groundless because any State is free to authorize whatever level of regulation it wishes among private actors. The state action defense would not be applicable in a State that did not clearly articulate and affirmatively express a state policy permitting the activity at issue. Here each state clearly permitted collective rate filing by rating bureaus.

FTC Amici also suggest that the Third Circuit decision will impair their ability to enforce state antitrust law. FTC Amici at 1, 3. The argument is baseless. The state action doctrine protects conduct from *federal* antitrust law if the State has decided to regulate a sector of its economy. The doctrine has no effect upon the scope of *state* antitrust law. Rather, state law doctrines of implied exemption or implied immunity may operate to remove state regulatory programs from state antitrust vulnerability. *E.g., Reese v. Associated Hospital Service, Inc.*, 45 Wis.2d 526, 173 N.W.2d 661 (1970). Such exclusions, however, depend entirely upon the actions of state legislatures and are not affected by the decisions of federal courts applying the state action doctrine.

FTC Br. at 26. The standard makes clear on its face that its principal focus is the existence of staffed and funded regulatory bodies with statutory duties to see that state regulatory policies are carried out. Under the Circuit Court reasoning, state legal mechanisms providing for judicial oversight of regulators' actions merely confirm the legitimacy of the State's program, by assuring that the regulatory duties imposed on state officials are not merely "precatory maxims," *New England*, 908 F.2d at 1072 n.10. Nothing in the standard remotely suggests that the existence of judicial review mechanisms alone would suffice as evidence of active supervision.

The Commission also argues that the judicial mechanisms here fall "far short of satisfying the active supervision requirement" because they resemble those in *Patrick*. FTC Br. at 25 (*quoting Patrick*, 486 U.S. at 104). It argues that under state law, officials in the four States here "have discretion whether and to what extent to investigate a particular rate filing," and because of such discretion mandamus would not be available to require state officials to see that rates conform to state policy. *Id.* at 25-26. However, the Commission ignores the mechanisms for administrative and direct judicial review of rate review matters that are embodied in the statutes of all four States. In each State, persons aggrieved by any rate filing are provided with specific statutory rights to require the regulator to hold a hearing or otherwise review the filing to determine that it comports with the rate criteria.[34] Once invoked, these regulatory duties narrowly

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[34] Ariz. Rev. Stat. Ann. § 20-378(B) (J.A. 170-171) (requiring a hearing if the regulator determines that the request is made in good faith and that the requester would be aggrieved if the grounds for the request are established); Conn. Gen. Stat. Ann. § 38-201p(a), (b) (J.A. 177-78) (requiring a hearing unless the regulator determines that there is no probable cause for the complaint or the request is made in bad faith); Mont. Code Ann. § 33-16-204 (J.A. 196-97) (requiring a hearing unless the regulator determines that there is no probable cause for the complaint or the request is

circumscribe any general discretion that otherwise might exist with respect to the regulator's review of particular rate filings, and would be enforceable by writ of mandamus even assuming the principles of mandamus law cited by the Commission and the FTC Amici.[35] Orders or decisions resulting from such administrative review are subject to state judicial review in the same fashion as other state administrative actions.[36] In short, the Third Circuit was correct in concluding that in each State the regulator's "duty to regulate pursuant to declared standards of state policy" was enforceable in the State's courts. (Pet. App. 30a, 33a, 35a, 36a.)

The existence of state agencies with the duty to review rates for compliance with substantive standards of state policy distinguishes this case from *Patrick*. In that case neither the state administrative agency nor the state judiciary had the authority to conduct more than a procedural review of the private conduct at issue. 486 U.S. at 101. Here, the existence of judicial review mechanisms serves to confirm the seriousness of these States in establishing a regulatory system where state administrative officials have the duty and authority to actively supervise private conduct according to substantive standards of state policy.[37]

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made in bad faith); Wis. Stat. Ann. § 227.42 (requiring a hearing for any person whose substantial interest is injured or threatened by agency action or inaction).

[35] *Cf. New England*, 908 F.2d at 1072 and n.10 ("The Massachusetts statute, as noted, requires officials to maintain just and reasonable rates, to act on complaints, to correct discriminatory rates, to consider various specified factors, and so on. . . . Such duties are enforceable by mandamus and other remedies in state courts.")

[36] Ariz. Rev. Stat. Ann. § 12-901 *et seq.*; Conn. Gen. Stat. Ann. § 4-183; Mont. Code Ann. § 2-4-701 *et seq.*; Wis. Stat. Ann. § 227.52.

[37] The FTC Amici assert that there was no active supervision in Montana and Wisconsin because search and examination rates in those states were intended to be the result of competition, not regulation. FTC Amici at 9, 13-15, 17-20. Though they attempt to frame it as an active supervision issue, this argument in truth is addressed to prong one of the *Midcal* test—whether Montana had a clearly articulated and affirmatively expressed policy to displace competition with regulation.

Because FTC Complaint Counsel conceded that Montana and Wisconsin authorized collective rate filing, the clear articulation requirement has never been in issue in this case. (Pet. App. 26a.) Even the Amici admit that the clear articulation prong is not before the Court. FTC Amici at 9, n.6. Their attempt to raise the issue indirectly at this late date should be ignored. *See* U.S. Sup. Ct. Rule 37.6 (*amicus curiae* brief must comply with Rule 24, which restricts a brief on merits from raising a new questions); *United Parcel Serv., Inc. v. Mitchell*, 451 U.S. 56, 60 n.2 (1981) (declining to consider argument of *amicus curiae* not raised by either of parties in Supreme Court or lower courts).

Moreover, FTC Amici are simply incorrect. Their reading of the Montana and Wisconsin statutes conflicts with the plain language of the statutes. Both States authorize cooperation between insurers in rate-making (Mont. Code. Ann. § 33-16-101 (J.A. 191); Wis. Stat. Ann. § 625.01), and explicitly authorize rating bureaus to make required rate filings with the state insurance departments (Mont. Code Ann. § 33-16-203 (J.A. 195); Wis. Stat. Ann. §§ 625.13 (1), 625.15 (J.A. 207-08)).

III. THE DECISION OF THE FEDERAL TRADE COMMISSION IMPROPERLY INTRUDED INTO STATE REGULATORY DECISIONS AND PROCEDURES.

The Third Circuit recognized the FTC's decision for what it was—an improper intrusion into state regulatory decisions and procedures.[38] The Third Circuit accurately

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[38] As the following indicates, on its face the FTC decision appears to intrude into state regulatory decisions far beyond inquiring whether the States "determine[d] whether the prices meet the State's regulatory criteria," the question it says is presented here. FTC Br. at (I). The FTC nonetheless has contended that the standard it urges in this Court is not different from that applied in its decision below. Reply Brief in Support of Petition for Certiorari at 1-2. Whichever view is correct, it is clear that the proper focus here is on the content of the FTC's decision. "The grounds upon which an administrative order must be judged are those upon which the record discloses that its action was based." *S.E.C. v. Chenery Corp.*, 318 U.S. 80, 87 (1943).

characterized the FTC's analysis of the active supervision issue:

> The FTC held that Arizona, Connecticut, Montana and Wisconsin failed *Midcal's* adequate supervision prong because the regulators in those states were unqualified, they approved rates that the FTC's commissioners would not have approved and they generally did not regulate to the degree that the FTC found desirable.

(Pet. App. 37a.) The Third Circuit held that the "root of the FTC's error" lay in its "insistence on sitting 'in judgment upon the degree of *strictness* or *effectiveness* with which a state carries out its own statutes.'" (Pet. App. 32a) (*quoting New England*, 908 F.2d at 1076, emphasis in original). It determined that even if the FTC's evaluation of the quality of regulation were correct, "its conclusions miss the point":

> Availability of the state action doctrine does not depend upon the quality of state supervision. The principles of federalism and state sovereignty that undergird the doctrine prohibit its selective application only where states act in a manner that a federal agency or federal court finds to be preferable.

(Pet. App. 37a.)

The FTC's administrative decision repeatedly reflects its willingness to substitute its own judgment and objectives for the substantive decisions of state regulators. Indeed, the FTC decision misstates the very purpose of the active supervision requirement, framing the objective of the requirement not in terms of state supervision for compliance with state regulatory policy, but rather as "ensur[ing] that the state agency has consciously considered the anticompetitive consequences of the activity for which private parties seek approval." (Pet. App. 55a.) Similar substitution of the FTC's competition objectives for the State's regulatory objectives occurs repeatedly in the FTC decision, leading the Commission to reject various state

regulatory choices as "impermissible" under federal antitrust principles, even though they further state regulatory policy. This fundamental error led the FTC to reject state regulatory decisions on such matters as 1) the manner of regulating insurer costs, 2) the use of historical rates as a justification for an initial bureau filing, 3) the allocation of administrative attention to minor filings, 4) the use of subsequent justifications and monitoring to assure compliance with the statutory rate criteria, and 5) staffing decisions.

1. In two States (Connecticut and Wisconsin), the Commission concluded that regulators' review and approval of filed rates was not proper because, in the FTC's view, "[t]here was no critical examination [by the regulator] of what lay behind those profit figures" and this was "fatal in and of itself" to Respondents' state action defense. (Pet. App. 57a, 59a.) This reasoning was not based on an absence of regulatory review and approval by the State—in Connecticut the regulator testified he approved the rate filing based on his conclusion that the proposed rates met the statutory standard, (*DiSanto* 2743-47, J.A. 77-78), and in Wisconsin the regulator testified that prior to approval he "gave the 1981 filing an intensive review" (*Wirtz* 1799, J.A. 20). Rather, the Commission determined that the departments in these States lacked the "wherewithal" to examine insurer expenses because "the department[s] lacked the authority to control insurer expenses they knew were excessive." (Pet. App. 59a.) As a result, the Commission reasons, the regulators could not "meaningfully" regulate a "critical" component of the ratemaking process. *Id.*

The Commission's analysis, focusing on the absence of direct regulatory authority to control these expenses, substitutes its own judgment regarding how rates should be regulated in these States for that of the legislatures. The legislatures decreed that insurance rates may not be excessive, and gave the departments the authority to reject

excessive rates. Conn. Gen. Stat. Ann. §§ 38-201c—201p (J.A. 172-80); Wis. Stat. Ann. §§ 625.11, 625.22 (J.A. 205, 208-09). The insurance codes do not authorize the department to directly regulate insurer expenses, but do specifically authorize the departments to consider past and prospective expenses in reviewing rate proposals. Conn. Gen. Stat. Ann. § 38-201c(b) (J.A. 172); Wis. Stat. Ann. §§ 625.11, 625.12 (J.A. 205-06, 206-07). The Commission does not suggest that the regulators in these States lacked power to attempt to force down the level of expenses by rejecting a proposed increase as excessive. The choice of how to design and implement a state regulatory program properly lies with the state legislature and regulators, not with the FTC.[39]

2. The Commission's willingness to dictate the substance of state regulatory decisions based on its own policy objectives is also reflected in its treatment of the initial rate filings made by the bureaus in Arizona in 1968 and Wisconsin in 1971. In these States the insurers, pursuant to then newly enacted state statutes, filed collective rates with the state regulators reflecting historical rates that had been charged by particular insurers in the open market. The collective rates were chosen in this fashion to comport with statutory provisions permitting the rates to be justified under the state regulatory criteria based on the experience of a title insurer doing business in the State. Ariz. Rev. Stat. Ann. § 20-377 (J.A. 169); Wis. Stat. Ann. § 625.12 (J.A. 206).

The Commission, invoking general federal antitrust principles, determined that "it is no excuse that the prices fixed are themselves reasonable" and therefore embraced its staff attorneys' argument that accepting prevailing rates is "not permissible." (Pet. App. 66a, 68a.) If, as

[39] Commissioner Azcuenaga, dissenting in part, concluded that "the Connecticut insurance department did all that was required of it by the statute" by its consideration of agency commission expenses when reviewing the bureau's filing. (Pet. App. 118a.)

this Court has said, the purpose of active supervision is to see that the State is carrying out its policies, it is difficult to understand why the Commission believed that it was "not permissible" for a regulator to accept filed rates that conformed to state policy.

3. The FTC treated the exercise of discretion by state regulators as a sign that the state regulators were not carrying out their regulatory responsibilities. The procedural rigidity demanded by the Commission's approach is reflected in its treatment of state oversight of various filings reflecting minor amendments or adjustments to the overall rate structure, or separate charges for particular policy endorsements. In Connecticut, Arizona and Wisconsin the Commission rested its finding of no active supervision in part on what it found to be insufficient oversight by state regulators of such filings. (Pet. App. 60a, 63a, 67a.)

Invoking the federal antitrust principle that "there is no *de minimis* exception to the antitrust laws for price-fixing," the Commission usurped the state regulatory function by holding it "impermissible" for a state regulator to determine to give lesser attention to filings with lesser economic importance. (Pet. App. 60a, 63a.) ("[W]hen a per se violation of the antitrust laws for price-fixing is involved, one need not judge economic import," Pet. App. 73a.) The obvious practical impact of the Commission's conclusion in this respect would be to force state regulators to expend more administrative energy on minor filings at the expense of giving less attention to significant filings. Such a result might satisfy the Commission's competition goals but it would do so at the expense of state regulatory policy.

4. The Commission's intrusion into the States' regulatory discretion is also reflected in its dissatisfaction with States that focused their supervisory activities on developing programs to monitor the economic effect of rates, following the acceptance by the departments of initial rate

filings by newly established rating bureaus. In Connecticut, Wisconsin and Arizona, after initial rate filings became effective the regulators, the bureaus and A.D. Little developed financial and statistical reporting plans designed to demonstrate the reasonableness of the rates on an ongoing basis. In Montana, the initial rate filing in 1983 was approved by the regulator subject to similar follow-up, but the bureau began to disintegrate before a report was produced.

Rather than recognizing these follow-up activities as indicia of active supervision, the Commission's analysis below ignored them or treated them as evidence that the regulators' review of the initial filings was inadequate. In Connecticut, the Commission decision makes no reference whatever to the later development of a reporting plan, focusing instead on its conclusion that there was no evidence, in the Commission's view twenty-three years later, that regulators' requests for information at the time of the initial rate filing were "answered satisfactorily." (Pet. App. 59a.) For Wisconsin and Arizona, the Commission's decision treats the eventual receipt by the regulators of reporting plan information justifying the filed rates as evidence of a "hands-off policy" by Wisconsin and proof that "there could not have been active supervision" by Arizona in the period before the information was received. (Pet. App. 62a, 68a.) For Montana the Commission took a slightly different tack, refusing to consider the regulator's requirement of statistical follow-up as evidence of active supervision, instead concluding from the failure of the reporting plan to be implemented that the rates *initially* "went into effect without being examined." (Pet. App. 76a.)

The Commission's reasoning, treating later regulatory follow-up as evidence of earlier insufficient state attention, puts state regulatory programs at risk which supervise through an ongoing program of oversight. Indeed the procedural rigidity demanded by the Commission in focus-

ing narrowly on pre-implementation state supervision of new rate filings appears to be useful principally as a means to subject the activity to federal antitrust liability, rather than to see that state regulatory policy is carried out.[40]

5. The Commission's decision makes clear in other ways as well its willingness to intrude on state regulatory discretion. The Commission accepted an argument suggesting that the staff of the Montana insurance department did not have the time to devote to rate review. (Pet. App. 75a.) Commissioner Strenio, the author of the majority opinion, opined (based upon his own prior "rate review experience" as a member of the Interstate Commerce Commission) that the Arizona insurance department had "no qualified personnel."[41] (Pet. App. 135a.) Indeed the

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[40] In *Southern Motor Carriers* this Court acknowledged the legitimacy and usefulness of collective rate filing through rating bureaus as part of a system of state rate regulation. 471 U.S. at 51. The FTC in its petition nonetheless displays overt animosity to this state regulatory alternative, asserting that the present case involves "horizontal price-fixing" that is "even more dangerous [to society] than ordinary price fixing" because of a state agency's monitoring of the "cartel." Pet. at 20-21. This same bias against the States' regulatory choices was reflected in the FTC decision below, as was candidly admitted by Commissioner Azcuenaga in her separate opinion: "The majority's apparent distaste for state-regulated price-fixing, which I share, perhaps carries more weight than it should in the majority's analysis of active supervision." (Pet. App. 113a.)

The FTC Amici assert that the Respondents admit fixing prices in the States at issue. Amici at 2. This is incorrect. The Respondents admit that they have jointly filed rates for search and examination services through state authorized rating bureaus. Contrary to the implications of these Amici that there was a broader agreement among the Respondents, the ALJ expressly found in the record in this case "not a hint of any collusive rate making activity outside of the rating bureaus." (Pet. App. 247a.)

[41] Commissioner Strenio asserts that "[t]he absence of sufficiently trained personnel seems substantively equivalent to not having an 'adequate system of regulation.'" (Pet. App. 135a, n.18) Dissenting Commissioner Azcuenaga observed that "the Commission should

free-wheeling approach applied by the Commission puts virtually no aspect of the State's regulatory organization or decisions beyond the scope of federal review under the active supervision requirement.

In sum, the practical, cumulative effect of the FTC's intrusive review of the merits of state regulation is a standard of active supervision that provides no guidance for future conduct and leaves private parties, who react in good faith to state regulation, at the mercy of inconsistent second-guessing by a federal antitrust tribunal. The factors which caused the Commission to arrive at its differing state-by-state results did not depend on the conduct of the Respondents, but rather upon the Commission's hindsight review of the action of the state regulators after the Respondents' rating bureau activities had occurred. The Third Circuit's rejection of the Commission decision on the grounds upon which it was rendered was clearly warranted.

IV. THE THIRD CIRCUIT DID NOT FAIL TO ACCORD PROPER DEFERENCE TO THE COMMISSION'S FINDINGS OF FACT.

The Commission wrongly contends that in finding active supervision to be present, the Court of Appeals "fail[ed] to accord proper deference to the Commission's findings of fact" by not "accepting the Commission's weighing of all the evidence and the credibility of witnesses." FTC Br. at 27-28. This argument mischaracterizes the nature of the Third Circuit's decision.

By its terms the FTC Act provides that "[t]he findings of the Commission *as to the facts*, if supported by evidence, shall be conclusive." 15 U.S.C. § 45(c) (emphasis added). Even the case principally relied upon by the Commission recognizes that this rule ends when appellate

decline to accept [Commissioner Strenio's] invitation to base our active supervision determinations in part on a review of the resumes of state regulatory personnel." (Pet. App. 123a.)

review involves ascertaining and applying the correct rule of law: "[T]he identification of governing legal standards *and their application to the facts found*—are, by contrast, for the [reviewing] courts to resolve." *F.T.C. v. Indiana Federation of Dentists*, 476 U.S. 447, 454 (1986) (emphasis added).[42]

The Third Circuit here rested its decision on its rejection of the legal standard of active supervision applied by the FTC. It held that "[a]vailability of the state action doctrine does not depend upon the quality of state supervision" (Pet. App. 37a) and that the Commission erred in using the active supervision requirement to sit "in judgment upon the degree of strictness or effectiveness with which a state carries out its own statutes." (Pet. App. 32a, *quoting New England*, 908 F.2d at 1076 (emphasis omitted).) Having determined that the Commission applied an erroneous standard of active supervision, the Third Circuit properly reviewed the administrative record as a whole to determine that active supervision existed under the correct legal standard.

The extensive factual discussion in the Commission's brief (FTC Br. at 28-30) shows that the fact findings that it claims were disregarded by the Third Circuit were, in each case, criticisms of the quality of the programs in those two States. The Commission does not dispute the facts relied upon by the Third Circuit to find the *existence* of a regulatory program under the legal standard it applied,[43] but simply argues that those facts fail to show

[42] Indeed this Court has emphasized the responsibility of reviewing courts to closely evaluate agency decisions which involve "a judgment as to the proper balance to be struck between conflicting [legal] interests" because they "would abdicate their responsibility if they did not fully review such administrative decisions." *N.L.R.B. v. Brown*, 380 U.S. 278, 291-292 (1965).

[43] The FTC admits that the Court of Appeals "did not expressly overturn any of the Commission's findings of fact." FTC Brief at 28, 29.

that the Arizona and Connecticut regulatory programs achieved the *quality* that the FTC's preferred standard would require.

For example, the Commission acknowledges that the Third Circuit is correct that following the 1968 rate filing in Arizona, state officials "sought information as to how a component of the rates was derived." FTC Br. at 28. The Commission simply argues that this finding fails to measure up to its own legal standard, because it does not show that "state officials determined that respondents' rates were consistent with the State's substantive criteria." *Id.* Similarly, the FTC acknowledges that the Third Circuit "relied on testimony by a state official that Connecticut reviews every rate it receives,"—a fact showing the existence of a regulatory program—but gave insufficient attention to the FTC's criticism "that state officials did not supervise insurer expenses." *Id.* at 29-30.

The Commission has not shown that the Third Circuit failed to defer to any finding of fact by the agency. The Court of Appeals properly exercised its role as a reviewing court to determine the correct rule of law and apply the law to the facts disclosed by the record.

CONCLUSION

The judgment of the United States Court of Appeals for the Third Circuit should be affirmed.

Respectfully submitted,

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APPENDIX

SUBSIDIARIES (EXCEPT WHOLLY OWNED SUBSIDIARIES) AND AFFILIATES OF STEWART TITLE GUARANTY COMPANY

The list of non-wholly owned subsidiaries and affiliates of respondent Stewart Title Guaranty Company included in the Appendix to Respondents' Brief in Opposition to the Petition for Certiorari remains current except for the additions and deletions listed below.

Additions:

Anchorage Title Company
Bachman-Stewart Title Co.
Fairbanks Title Company
Landata of Kansas City
Local Express
Professional Real Estate Tax Service
South Texas Delivery
Star Courier
Star Delivery, Inc.
Stewart Title & Settlement Services Inc.
Stewart Title Company of California
Stewart Title Company of Riverside County
Stewart Title of Central Nevada
Stewart Title of Fairfax
Stewart Title of Kansas City
Stewart Title of Snohomish County
Stewart-Fidelity Title Company
Stewart-Princeton Abstract
Stewart-West Coast Title

Deletions:

American Surveying of New England
Environmental Information Systems

Intercounty Abstract Co. d/b/a Stewart Title of New Hampshire
Island Title Exchange, Inc.
Landata Inc. of New England
Landmark Title, Inc.
Meyerdirk Title Co. (Kansas)
Stewart-Fidelity Title Company
Stewart Metro Title Corporation
Stewart of Bayshore
Stewart-Princeton Abstract
Stewart Tax Service
Stewart Title Company of Michigan
Stewart Title Co. of Palestine
Stewart Title of Birmingham, Inc.
Stewart Title of Central Jersey, Inc.
Stewart Title of Columbia
Stewart Title of Fort Lauderdale, Inc.
Stewart Title of Greater Washington, Inc.
Stewart Title of Indianapolis, Inc.